

Internal Revenue Service

Number: **200939011**
Release Date: 9/25/2009

Index Number: 302.03-00

Department of the Treasury
Washington, DC 20224

[Third Party Communication:
Date of Communication: Month DD, YYYY]
Person To Contact: , ID No.
Telephone Number:

Refer Reply To:
CC:CORP:4
PLR-119843-09
Date:
June 24, 2009

Legend

Corporation =

Date 1 =

Business A =

Taxpayer =

Son 1 =

Son 2 =

Son 3 =

b =

c =

d =

e =

f =

g =

y =

Dear :

This letter responds to your letter dated March 31, 2009, in which you requested rulings under section 302(b)(3) of the Internal Revenue Code. The information submitted in that letter and later correspondence is summarized below.

The rulings contained in this letter are based upon information and representations submitted by Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Summary of Facts

Corporation uses the accrual method of accounting and files its federal income tax return on a fiscal year ending on Date 1. Corporation conducts Business A. Currently, Corporation has outstanding b shares of voting common stock which are owned as follows:

Shareholder	Number of Shares Owned
Taxpayer	<u>c</u>
Son 1	<u>d</u>
Son 2	<u>d</u>
Son 3	<u>d</u>

Taxpayer is the father of Son 1, Son 2, and Son 3.

Taxpayer is a director, an employee, and the President of Corporation. Son 1 is a director, a former employee, and the Secretary of Corporation. Son 2 is a director, an employee, and the Vice President of Corporation. Son 3 is a director, an employee, and the Secretary/Treasurer of Corporation.

Taxpayer wants to retire and allow Son 2 and Son 3 to operate and control Corporation. Son 1 no longer wants to be involved with Corporation. As a result, Corporation will redeem all of Taxpayer and Son 1's Corporation stock. Prior to Corporation's redemption of Taxpayer and Son 1's shares, Taxpayer will give Son 2 and Son 3 e shares each of Corporation stock (the "Gifts"). Following Taxpayer's Gifts to Son 2 and Son 3, Corporation's common stock will be owned as follows:

Shareholder	Number of Shares Owned
Taxpayer	<u>f</u>

Son 1	<u>d</u>
Son 2	<u>g</u>
Son 3	<u>g</u>

Shortly after the Gifts, Corporation will redeem all of Taxpayer's remaining shares and Son 1's shares in exchange for 15-year promissory notes. The principal amounts of the promissory notes are based on a per share price of \$y. Following the redemption, the shares of Corporation stock will be owned as follows:

Shareholder	Number of Shares Owned
Son 2	<u>g</u>
Son 3	<u>g</u>

After the redemption, Taxpayer will no longer be an employee, a director, or the President of Corporation. However, Taxpayer will be a creditor of Corporation and an account holder in Corporation's 401(k) plan.

Representations

Taxpayer makes the following representations:

- a) There are no outstanding options or warrants to purchase Corporation stock, nor are there any outstanding debentures or other obligations that are convertible into Corporation stock or would be considered Corporation stock.
- b) In no event will the last payment of the promissory note Taxpayer will receive in exchange for his Corporation stock (the "Promissory Note") be made more than 15 years after the date of issuance of the Promissory Note.
- c) None of the consideration from Corporation, including interest, consists entirely or partly of Corporation's promise to pay an amount that is based on, or contingent on, future earnings of Corporation, an amount that is contingent on working capital being maintained at a certain level, or any other similar contingency.
- d) The Promissory Note will not be subordinated to the claims of general creditors of Corporation.
- e) In the event of a default on the Promissory Note, no shares of stock will revert to or be received by Taxpayer nor will Taxpayer be permitted to purchase stock at public or private sale.
- f) No shareholder of Corporation has been or will be obligated to purchase any of Taxpayer's shares of stock to be redeemed.

- g) The redemption of Taxpayer's Corporation stock is related to the Gifts, as well as the complete redemption of Son 1's Corporation stock. Otherwise, the redemption described in this ruling request is an isolated transaction.
- h) There have been no redemptions, issuances, or exchanges by Corporation of its stock in the past 5 years.
- i) Corporation has no plan or intention to issue, redeem, or exchange additional shares of its stock.
- j) None of the stock to be redeemed was acquired by the Taxpayer within the 10-year period preceding the redemption from a person whose stock would be attributed under § 318(a) of the Code to the Taxpayer at the time of the redemption.
- k) Throughout the 10-year period following the redemption, Taxpayer will not have an interest in Corporation, including an interest as officer, director, or employee (other than an interest as a creditor as described in § 1.302-4(d) of the Income Tax Regulations, and constructive ownership under § 318(a)(1) of the Code).
- l) Taxpayer will execute and file the agreement required by § 302(c)(2)(A)(iii) of the Code with respect to the acquisition of any interest in Corporation within 10 years from the date of redemption.
- m) None of the stock to be redeemed is "section 306 stock" within the meaning of § 306(c) of the Code.
- n) There are no declared but unpaid dividends, or funds set apart for dividends, on any of the stock to be redeemed.
- o) At the time of the exchange, the fair market value of the consideration to be received by Taxpayer will be approximately equal to the fair market value of the Corporation's stock to be exchanged therefor.
- p) The price to be paid for Corporation's stock to be redeemed will not result in a loss with respect to those shares of stock.
- q) The redemption of Corporation stock (i) is not a disposition of personal property on the installment plan by a person who regularly sells or otherwise disposes of personal property on the installment plan and (ii) is not a disposition of personal property of a kind required to be included in the inventory of any redeemed shareholder at the close of the taxable year.

Rulings

Based on the information submitted and on the representations set forth above, we rule as follows:

- 1) The gift of Corporation stock by Taxpayer to Son 2 and Son 3 did not have as one of its principal purposes the avoidance of federal income tax within the meaning of §302(c)(2)(B) of the Code (Rev. Rul. 77-293, 1977-2 C.B. 91).
- 2) Provided that Taxpayer files the agreement described in section 302(c)(2)(A)(iii) in accordance with section 1.302-4(a), and the conditions stated in section 302(c)(2)(A)(i) and (ii) are satisfied, section 318(a)(1) will not apply, and the redemption of all of Taxpayer's shares of Corporation stock will be a "complete termination" of Taxpayer's interest in Corporation within the meaning of section 302(b)(3). The amount distributed in the redemption will be treated as a distribution in full payment in exchange for the stock surrendered as provided in section 302(a).
- 3) As provided in section 1001, Taxpayer will realize and recognize gain on the redemption of the Corporation shares of stock. For each share of stock surrendered, gain will be measured by the difference between the redemption price and the adjusted basis of such share as determined under section 1011. Provided that Corporation stock is a capital asset in the hands of Taxpayer, the gain will constitute capital gain subject to the conditions and limitations of Subchapter P of Chapter 1 of the Code. Pursuant to § 267 of the Code, no loss will be allowed.
- 4) Provided the redemption of the Corporation stock held by Taxpayer and Son 1 is not performed in satisfaction of a primary and unconditional obligation of a nonredeemed shareholder to acquire the Corporation stock held by said shareholders (see Rev. Rul. 69-608, 1969-2 C.B. 42), the redemption will not cause any dividend income to be realized or constructively received by any nonredeemed shareholder (see *Holsey v. Commissioner*, 258 F.2d 865 (3rd Cir. 1958), acq., Rev. Rul. 58-614, 1958-2 C.B. 920).
- 5) Corporation will not recognize gain or loss on the distribution of its own promissory notes in redemption of its stock (section 311(b)).
- 6) Taxpayer will qualify to report the gain on the redemption of Taxpayer's Corporation stock using the installment method under § 453(b) of the Code. In the event the Promissory Note is cancelled or otherwise becomes unenforceable, the Promissory Note shall be treated as if it were disposed of for fair market value, which shall be treated as not less than its face amount (section 453B(f)(1) and (2)).

Caveats

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

Procedural Statements

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

Marie C. Milnes-Vasquez
Senior Technician Reviewer, Branch 4
Associate Chief Counsel (Corporate)

cc: